ORAL TESTIMONY OF ROBERT D. BROEKSMIT
BEFORE THE FEDERAL HOUSING FINANCE BOARD
ON BEHALF OF THE MORTGAGE BANKERS ASSOCIATION

January 23, 2004

Good morning, Mister Chairman and members of the Finance Board.

I am Robert Broeksmit, President and Chief Operating Officer of B.F. Saul Mortgage Company, a subsidiary of Chevy Chase Bank, F.S.B., in Bethesda, Maryland, and a member of the Federal Home Loan Bank System.

Thank you for inviting the Mortgage Bankers Association to discuss whether changes to your regulations or revisions to the Federal Home Loan Bank Act would enhance governance of the Banks.

We think you are doing the right thing in looking for ways to improve the safety and soundness of the System through effective supervision of the activities of the Banks. After the unprecedented mortgage volume of the last year and the unusual level of focus on the housing GSEs, the time is right for a reevaluation.

That reevaluation should be undertaken with a view toward enhancing the successes of the recent past while minimizing any risks that have come with them. MBA believes it is critical that the Board focus its efforts as much on the former as on the latter.

Specifically, we urge that you preserve and encourage the prudent development of the Mortgage Partnership Finance and Mortgage Purchase Program initiatives. We believe that these programs represent <u>the</u> major step in the evolution of the Bank System in the last decade. The continued health of the mortgage programs is essential to the ability of the Banks to satisfy the statutory mandates of the Federal Home Loan Bank Act.

MBA's members are the partners of the Banks in their mortgage acquisition programs, and through these programs, the Banks have added an important element of competition in the secondary mortgage market.

We believe that the MPF and MPP programs have been useful for your members and for homebuyers, and have created vital funds for affordable housing. Not only have the Banks

contributed to lowering mortgage costs through adding another outlet for mortgages, they have developed an innovative risk sharing mechanism. That kind of innovation is the basis for progress in continuing to make the mortgage system even more efficient.

The positive achievements the Banks have accomplished for their members through the mortgage programs are extensive. The large members of the Banks generate the critical mass necessary to make the mortgage programs viable, and they appreciate having another execution option for the sale of their mortgages.

Smaller members of the System also benefit in a variety of ways. Small lenders tend to know their customers. They are willing to accept the credit risk on their mortgage loans instead of paying MBS guarantee fees they see as high compared to the real risk of loss. The Banks' mortgage programs give them that option. The mortgage programs also allow small lenders to maintain their customer relationships through servicing their loans, where many competing execution options either impose minimum delivery levels for retaining servicing or require that the servicing be released. In these and other ways, the Banks have used the mortgage programs to provide broader choice, more business opportunity and additional mortgage funding for members.

For homebuyers, more competition means lower cost of homeownership. And for those in need of affordable housing, ten percent of the profits generated by the MPF and MPP programs are directed to serving that population. Those profits have allowed the Banks to be among the largest private sources of funds for affordable housing.

The challenge for the Finance Board is defining the line between prudent regulation and chilling micro-management or unnecessary risk aversion.

This task is not static because the Banks have grown significantly in the last ten years, and the categories of assets on their balance sheets have changed dramatically and have become more complex. In addition, the industry as a whole is struggling to incorporate changing accounting standards into the presentation of our financial results. MBA believes it is

important that the Finance Board distinguish between unintended accounting consequences and risk-prone investment practices as you assess the performance of the Banks.

In your announcement of this hearing, you referenced the June report of your staff and the conclusions reached with regard to the Boards and the operations and risk management practices of the Banks. MBA has the following observations to make about governance of the Banks:

- **First, the staff notes that some of the members of the Boards of Directors of the Banks lack experience in capital markets and some also do not have the time, training or financial incentive to acquire a working knowledge of the business of the Banks. We believe that the Finance Board should establish baseline standards for qualifications for members of the Boards of Directors of the Banks.**
- **The staff also mentions technology investment, including the development of risk management models and the hiring of experienced staff as an area that requires more attention from some Banks. MBA believes that to preserve**

the financial health of the Banks, the Banks themselves must all be brought to a standard of competent evaluation of the risks of their business practices. Here again, MBA believes it is the role of the Finance Board to establish the benchmarks which the Banks must reach. The Finance Board itself must have the most up-to-date tools for performing its regulatory function and determining how the Banks should perform their internal due diligence. In order to be up to the necessary standard, the Finance Board will need to evaluate its own expenditures for risk management, training and evaluation to determine if this critical function is adequately funded.

- **MBA also suggests that the Finance Board examine the merits of a relationship between the Finance Board and the Federal Financial Institutions Examinations Council, the members of FFIEC individually, and with the Office of Federal Housing Enterprise Oversight. All of these regulators and the Finance Board are engaged in the difficult work of regulating sophisticated banking entities,**

and we believe that the sharing of expertise would be beneficial.

In summary, MBA believes that the Finance Board should handle its responsibility as a regulator with the objective of allowing the Banks to serve their mandate in a safe and sound way by establishing the quality control standards to which the Banks must adhere. Those standards should be devised to shore up any management shortcomings that some of the Banks might have on their Boards or in their internal management. The Finance Board then must hold the Banks and their Boards to the prescribed standards.

But the Banks have done great things for housing in recent years, and they made money for their shareholders at the same time. We urge the Finance Board to act in such a way that the Banks can continue to serve the needs of their shareholders and the needs of the American public in the creative and effective manner that has characterized the Banks since the inception of the MPP and MPF programs.